Petition

81-713

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No. 81-_____

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

JAMES MCHUGH CONSTRUCTION CO., *Petitioner*

v.

COMPTROLLER OF THE TREASURY, RETAIL SALES TAX DIVISION FOR THE STATE OF MARYLAND, *Respondent*

PETITION FOR WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE STATE OF MARYLAND

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PRESS OF BYRON S. ADAMS PRINTING, INC., WASHINGTON, D.C.

QUESTIONS PRESENTED

1. May a party to an interstate compact, pursuant to Article I, Section 10, Clause 3 of the United States Constitution, unilaterally amend its sales tax law so as to subject contractors performing contracts for the compact to sales taxes to which they were not subject when the compact was entered into?

2. Does application of said unilateral amendment of the Maryland sales tax law to contractors performing contracts for the compact, impair the State's contract obligation as a party to the compact under Article I, Section 10, Clause 1 of the United States Constitution?

3. Does collection of said sales tax from Petitioner impair or infringe upon the title, rights, privileges and immunities of Petitioner under the United States Constitution?

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REPORTS AND OPINIONS ISSUED BELOW

James McHugh Construction Co. v. *Comptroller*, 431 A.2d 1353 (Md. 1981) 6, 8-10

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JURISDICTION

The Judgment sought to be reviewed was entered July 17, 1981. The statutory provision conferring jurisdiction on this Court to review the judgment in question by writ of certiorari is 28 U.S.C. § 1257(3). That statute provides in pertinent part:

> Final judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> (3) By writ of certiorari, . . . where the validity of a State statute is drawn in question on the ground of its being repugnant to the Constitution, treaties or laws of the United States, or where any title, right, privilege or immunity is specially set up or claimed under the Constitution, treaties or statutes of, or commission held or authority exercised under, the United States.

Constitutional provisions involved here are U.S. Const. art I, § 10, cl. 3:

> No state shall, without the consent of Congress . . . enter into any Agreement or Compact with another State . . .

and U.S. Const. art I, § 10, cl. 1:

> No State shall . . . pass any . . . law impairing the obligation of contracts. . . .

This case challenges an application of Maryland law imposing a tax in derogation of an interstate compact which compact had been entered into with the consent of the United States Congress pursuant to U.S. Const. art I, § 10, cl. 3. Since the tax law was enacted subsequent to the date when the compact came into being, the tax law conflicts with the compact, constituting an impairment of a contractual obligation in violation of U.S. Const. art I, § 10, cl. 3. Imposition of the tax on Petitioner impaired and infringed upon its title, rights, privileges, and immunities under the Constitution of the United States.

STATEMENT OF THE CASE

The Decision Below

James McHugh Construction Co. (hereafter "Petitioner")[1] seeks a writ of certiorari to the Maryland Court of Appeals, the highest court of the State of Maryland. On July 17, 1981, that court affirmed a decision of the Circuit Court for Montgomery County, Maryland, in favor of the Comptroller of the Treasury of Maryland (hereafter "Respondent"), denying petitioner's request

[1] Petitioner has no parent companies. Burton Street Corporation and Engineered Concrete Form Corporation are affiliate companies. Petitioner has no partially owned subsidiaries.

for refund of sales and use taxes levied and collected on property petitioner had incorporated into the Maryland portion of the Washington area subway system.[2] In its decision, the Maryland Court of Appeals concluded that Maryland is authorized by the language of the Washington Metropolitan Area Transit Authority ("WMATA") Compact ("Compact") to tax contractors performing construction, repair or alteration of real property owned by WMATA, and that imposition of such a tax is not in conflict with the Compact. But that Court ignored the constitutional issues raised by petitioner at all stages.

The Background

The State of Maryland,[3] the Commonwealth of Virginia, and the District of Columbia entered into the Compact for the purpose of establishing a subway system in the Washington, D.C. area. The Congress of the United States duly consented in accordance with Article I, Section 10, Clause 3, of the Constitution of the United States.[4] The Compact created an entity called WMATA which entered into contracts with companies like Petitioner for the purposes of actually building the subway system.

Pursuant to its contract with WMATA, Petitioner paid sales and use taxes on materials it purchased which were physically incorporated into the subway tunnel. Such taxes were not payable by contractors on public construction projects or on this project under Maryland tax law

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[2] The decision of the Maryland Court of Appeals is attached as Appendix A. The decision of the Circuit Court for Montgomery County is attached as Appendix B. The decision of the Maryland Tax Court is attached as Appendix C and the decision of the Comptroller is attached as Appendix D.

[3] Maryland Transp. Code Ann., § 10-204.

[4] Act of November 6, 1966, Public Law 89-774, 80 Stat. 1324.

prior to ratification of the Compact. After Compact ratification, the Maryland sales tax law changed. Petitioner was for the first time subject to sales and use taxes on materials purchased for incorporation in the subway system.

The Procedural History

Petitioner applied to the Comptroller of the Treasury of the State of Maryland for a refund, arguing that Maryland could not unilaterally amend its sales tax law so as to impose a new sales tax to which WMATA contractors were not subject when the Compact was formed. In its memorandum in support of its applications for refund, petitioner stated that applying the tax to WMATA contractors was improper because:

"1. The new tax burdened the Company and adversely affected the broad public and governmental purposes which the Company was to carry out.

"2. It impaired and infringed upon the title, rights, privileges, and immunities of petitioner under the Constitution of the United States and under the Compact; and

"3. Paragraph 78 of the Compact exempted WMATA contractors from payment of sales and use taxes to the State of Maryland."

Petitioner's Memorandum in Support of Refund at 7-22.

The Comptroller denied petitioner's application on July 23, 1976. *See* App. D. Petitioner appealed to the Maryland Tax Court, raising the identical issues. *See* App. C.

Respondent expressly denied that the Tax Court should review the questions set forth by Petitioner and

asserted in its brief that the only questions presented for consideration were:

"a. Whether the Compact precludes the Respondent from applying Chapter 452 of the Laws of Maryland (1968) to contractors with WMATA.

"b. Whether paragraph 78 of the Compact exempts Petitioner, as a contractor with WMATA, from payment of sales and use taxes."

Brief for Respondent at 2-14.

Before the Tax Court, Respondent correctly stated the basic issue — whether or not the new tax was valid:

> If McHugh is correct as to either of its contentions, *i.e.*, that the transactions are exempt under the terms of the Compact or that, if not exempt, Maryland has exceeded its authority, McHugh will not be responsible for the payment of the taxes in question.

Brief for Respondent at 2-3.

On February 23, 1979, the Maryland Tax Court failed to meet this basic issue. It affirmed Respondent, explaining *inter alia* that "we need not reach these legal questions for we find, as a matter of fact, that the Act [amending the sales tax law] has not burdened the Compact in the manner claimed." *See* App. C at p. 2.

Petitioner again raised the same issues before the Circuit Court for Montgomery County, Maryland. On March 10, 1980, that Court dismissed the appeal in an Opinion and Order attached as App. B.

The Maryland Court of Appeals itself never dealt with the constitutional issues either, although they were repeatedly raised below and clearly were before it. The highest court of the Maryland held that:

> Because Maryland is expressly authorized by the plain language of § 10-203, Art. VII, of the Compact

> to tax contractors performing construction, repair, or alteration of real property owned by the Authority, the 1968 Amendment to Art. 81, § 326(a) which imposed such a tax is not in conflict with the Compact. The contractor is not entitled to a sales tax refund. Accordingly, we shall affirm.

James McHugh Construction Co. v. *Comptroller*, 431 A.2d 1353, 1360 (Md. 1981) ("*McHugh*").

Reasons for Granting Writ

Maryland has undermined the integrity of an interstate compact through unilateral amendment of state law in derogation of the Compact's terms. As Justice Frankfurter said in *West Virginia* v. *Sims*, 341 U.S. 22 at 26, 95 L.Ed. 713 at 721 (1951) ("*Sims*"), concerning a purported conflict between state law and a compact:

> That these are issues which give this Court jurisdiction to review the State court proceeding, 28 U.S.C. § 1257, needs no discussion after *Delaware River Joint Toll Bridge Com.* v. *Colburn*, 310 U.S. 419, 427, 84 L.Ed. 1287, 1289, 60 S. Ct. 1039.

The case at bar represents the most significant threat to an interstate compact since *Sims* was decided in 1951. In *Sims*, the state court had found that an interstate compact violated a state appropriation law, and that therefore state approval of the compact was invalid. Here, Maryland has taxed the property under a compact after the compact's ratification and in clear violation of compact terms.

Just as Justice Frankfurter explained in *Sims*, the Supreme Court does not decide the meaning of a state statute as applied to a state appropriation, this Court need not decide the validity of Maryland's amendment to its tax law insofar as the amendment affects public contractors generally. The issue here involves only contractors working pursuant to the Compact. Whether Maryland

may amend tax laws to burden *Compact* contractors is an important question that should be decided by this court, for the same reason that this Court addressed the challenge to the interstate compact in *Sims*.

Mr. Justice Reed explained in a concurring opinion why a state law like Maryland's post-compact sales tax law must give way to the supremacy of a compact.

> Under the Compact Clause, however, the federal questions are the execution, validity and meaning of federally approved state compacts. The interpretation of the meaning of the compact controls over a state's application of its own law through the Supremacy Clause and not by any implied federal power to construe state law. *Sims*, 331 U.S. at 334, 95 L.Ed. 725.

Here, the highest court of Maryland construed a sales tax law as being applicable to WMATA contractors. The sales tax did not exist on materials incorporated in public projects prior to the effective date of the Compact. The later-enacted Maryland sales tax was expressly prohibited by paragraph 78 of the Compact:

> It is hereby declared that the creation of the Authority and the carrying out of the corporate purposes of the Authority is in all respects for the benefit of the people of the signatory states and is for a public purpose and that the Authority and the board will be performing an essential governmental function, including, without limitation, proprietary, governmental and other functions, in the exercise of the powers conferred by this title. Accordingly, *the Authority* and the board *shall not be required to pay taxes* or assessments *upon any of the property acquired by it or under its jurisdiction, control, possession or supervision* or upon its activities in the operation and maintenance of any transit facilities or upon any revenues therefrom and the property and income derived therefrom shall be exempt from all federal, state,

> District of Columbia, municipal and local taxation. *This exemption shall include,* without limitation, all motor vehicle license fees, *sales taxes* and motor fuel taxes.

Compact, § 10-204 ¶ 78. (Emphasis supplied.)

The Maryland Court of Appeals side-stepped the issue of whether or not it could impose a new tax on WMATA contractors. It held ". . . there is no express provision in the Compact granting . . . exemption to contractors from sales tax on materials acquired by them for the Authority." *McHugh,* 431 A.2d at 1357. The Court of Appeals cited Art. VII, § 203, for the proposition that the Compact correctly permitted the sales tax at issue here. That provision stated in relevant part:

> *Nothing herein shall be construed to amend, alter, or in any wise affect the power of the signatories* and the political subdivisions thereof *to levy and collect taxes* on the property or income of any person or company subject to this Compact or upon any material, equipment or supplies purchased by such person or companies. . . .

McHugh 431 A.2d 1353 at 1357. (Emphasis added.)

However, this provision must be read in conjunction with the previous citation from the Compact, to the effect that states were permitted to continue levying and collecting the same income and property taxes as before Compact ratification, but were *not* permitted to levy and collect new property taxes directed specifically at Compact contractors. Even more importantly, the construction suggested by the Maryland Court of Appeals must be struck down for the effect it has of permitting a state like Maryland to cripple implementation of Compact purposes by imposing new terms after Compact ratification.

The Maryland Court of Appeals had previously acknowledged that a contractor is entitled to precisely the sales tax exemption sought here. "The exemption . . . depends upon the *use* to which the property is put, and not upon the immunity of the user. . . ." *John McShain, Inc.* v. *Comptroller,* 202 Md. 68 at 72-74, 95 A.2d 473 at 474-75 (1953) (*"McShain"*). There, an exemption from sales tax in favor of charitable purposes, such as nonprofit hospitals, was held to apply to materials purchased by contractors who were constructing the National Institutes of Health. The building materials in *McShain* are on all fours with the subway materials in *McHugh.*

In *McShain,* the Maryland high court ruled that the National Institutes of Health are entitled to the tax exemption, and their contractors are exempt from a sales tax on materials used in the construction. Likewise here, WMATA was exempt from tax under the Compact, and Petitioner should have been exempted from tax under the Compact as well. But the Maryland Court of Appeals ruled in *McHugh* that on the contrary, the exempt enterprise is entitled to sales tax exemption, but the contractor working for the compact must pay sales tax on materials it uses. Thus *McShain* and *McHugh* are inconsistent. The *McHugh* decision below is plainly wrong, insofar as it permits Maryland to tax materials the state had previously determined by compact would be exempt from taxation. The *McShain* decision was correctly decided, and must remain the law of Maryland at least as far as Compact contractors are concerned.

The Maryland Court of Appeals summarily referred to *Delaware River and Bay Auth.* v. *Carello,* 43 Del. Ch. 213, 220-21, 222 A.2d 794, 799 (1966) (*"Carello"*). The Court called *Carello* "inapposite" because that case, "unlike here," involved a statute "in conflict with an express

provision of a compact." *McHugh*, 431 A.2d at 1360, ft. 6. Yet, the *Carello* case involved precisely the issue involved here — unilateral legislation subsequent to the date on which a compact pursuant to Article I, Section 10, Clause 3, of the United States Constitution had come into being. The Delaware River and Bay Authority ("Authority") was created by compact. After Delaware legislation granted collective bargaining rights to public employees in Delaware, certain employees of the Authority sought bargaining rights pursuant to the new law. The Authority contended, and the Delaware court agreed, that the unilateral action by the State of Delaware in according the collective bargaining rights to public employees was not binding on the Authority. The Delaware compact had no provision barring collective bargaining *in haec verba*, but merely provided that ". . . no additional duties or obligations shall be undertaken by the Authority under the law of either State or of Congress without authorization by the law of both states." *Carello*, 222 A.2d at 796.

The Delaware court concluded that ". . . where an interstate compact exists, one state to such an arrangement may not unilaterally legislate so as to place burdens on the compact in question." *Id.*, 222 A.2d at 798. The same conclusion applies here. The duty to bargain collectively imposes an impermissable burden on a compact. A tax on materials used in constructing WMATA's subway is even more of a burden.

Here, no attention was given by the Maryland Court of Appeals to the question of who "bore the burden of the tax" because the Court concluded it need not decide that question. *McHugh*, 421 A.2d at 1360, ft. 7. However, this also is a question deserving consideration.

Based on *Sims*, *McShain*, *Carello*, and the importance of preserving the inviolate character of interstate com-

pacts under the United States Constitution, certiorari should be granted to review the arbitrary action of the State of Maryland. WMATA contractors were not subject to taxes on materials incorporated into subway construction when WMATA came into being. Therefore, subsequent and unilateral taxation must be declared invalid as to those materials. Failure to review this taxation by the State of Maryland will permit the State to override its solemn undertaking as a party to an interstate compact, and will set a dangerous precedent.

Conclusion

Wherefore, petitioner respectfully prays that a writ of certiorari be granted.

Respectfully submitted,

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APPENDIX

APPENDIX A

IN THE COURT OF APPEALS OF MARYLAND

No. 57

September Term, 1980

JAMES MCHUGH CONSTRUCTION COMPANY

v.

COMPTROLLER OF THE TREASURY,
RETAIL SALES TAX DIVISION

MURPHY, C.J.
SMITH
DIGGES
ELDRIDGE
COLE
DAVIDSON
RODOWSKY, J.J.

Opinion By Davidson, J.

(Filed: July 17, 1981)

This case presents the question whether a 1968 amendment to Maryland Code (1957, 1980 Repl.Vol.), Art. 81, § 326(a) conflicts with Art. XVI-78 of the Washington Metropolitan Area Transit Authority (WMATA) Compact, Maryland Code (1977, 1980 Repl.Vol.) §10-204 of the Transportation Article.[1]

[1] The WMATA Compact, adopted and codified in 1965 as Md. Code (1957, 1965 Repl.Vol.), Art. 41, § 317-1 through § 317-86, constituted Title III of the Washington Area Transit Regulation Compact (WATRC), adopted and codified in 1959 as Art. 41, § 268 through § 317. In 1977, WATRC was recodified as Md. Code (1977, 1980 Repl.Vol.) §10-203 of the Transportation Article and the WMATA Compact was recodified as §10-204 of the Transportation Article. No substantive changes were made at the time of the recodification. *See* Revisor's Notes to §10-203 and §10-204.

Maryland, Virginia and the District of Columbia entered into the Compact[2] for the purpose of regulating transit on a coordinated basis throughout the area by establishing a common agency designed to alleviate transit and traffic problems in the metropolitan area. The Compact declared that the Authority was created for a public purpose and should not be required to pay taxes upon any property acquired by it. §10-204, Art. XVI-78. In addition, it provided that the signatory states' power to levy and collect taxes upon any material, equipment, or supplies purchased by any company subject to the Compact was not affected. §10-203, Art. VII.

At the time the WMATA Compact was adopted in 1965, the Retail Sales Tax Act, Art. 81, § 324 through § 371, contained an exemption for the State of Maryland. Article 81, § 326(a) provided:

> "The tax hereby levied shall not apply to the following sales:
>
> (a) State sales. — Sales to the State of Maryland or any of its political subdivisions."

Tax Laws and Regulations, Rule 70, promulgated by the Comptroller of the Treasury, then provided that contractors performing jobs for the State were not required to pay a sales tax on materials and supplies to be incorporated into the job.[3]

In 1968, Art. 81, § 326(a) was amended (1968 Amendment) to subject previously exempt contractors to a sales tax on property to be used for the construction, repair, or altera-

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[2] Throughout this opinion, the term "Compact" includes both the WATRC Compact, §10-203, and the WMATA Compact, §10-204.

[3] Rule 70 provided in pertinent part:

> "Contractors who are performing jobs for the State of Maryland or any of its political sub-divisions or a non-profit religious, charitable, scientific, literary or educational institution or organization located within the State of Maryland on a lump-sum basis are not required to pay the tax on materials and supplies which will be incorporated into the job."

tion of real property owned by the State of Maryland. As amended, § 326(a) provides:

> "The tax hereby levied does not apply to the following sales:
>
> (a) State sales. — Sales to the State of Maryland or any of its political subdivisions. *Provided that this subsection shall not be construed or applied to exempt any sale, otherwise taxable* under this subtitle, of tangible personal property *to contractors or builders* to be used for the construction, repair or alteration of real property, on contracts advertised for bids after July 1, 1968." (Emphasis added.)

In 1968, Rule 70 was amended to provide that contractors performing jobs for the State of Maryland and must pay a sales tax on all of their purchases. Tax Rules and Regulations, Rule 70; Rule 70A.[4]

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[4] Amended Rule 70 provides:

> "Contractors and subcontractors performing construction contracts for the State of Maryland or any of its political subdivisions or the U.S. Government or its agencies, under contracts which are bid after July 1, 1968, must pay the tax on all their purchases."

Rule 70A provides in pertinent part:

> "Contractors and subcontractors performing construction contracts for non-profit religious, charitable or educational institutions or organizations for use in carrying on the work of the non-profit institution or organization may purchase tax free the materials which will actually be incorporated into and remain a part of the finished job. Nothing in this Rule 70A shall apply to contracts with Federal, State or Local Governments or Agencies."

COMAR 03.06.01.53, effective 1977, provides in pertinent part:

> "A. The sale of tangible personal property to a person who will use or resell it in the form of real property is taxable. Therefore, a person who constructs, improves, alters, or repairs real property shall pay the tax on all materials he purchases, which will be incorporated into real property in such a manner that the materials will lose their identity as tangible personal property.
>
> * * *
>
> D. A person who, because of a contractual obligation, purchases material which will be incorporated into the real property

In 1974, the petitioner, James McHugh Construction Company (contractor), entered into a contract with WMATA to construct a portion of a subway system located in Bethesda, Maryland. Thereafter, the contractor paid sales tax on all materials incorporated into the subway structure.

The contractor filed various claims for the refund of the paid sales tax. The Comptroller of the Treasury denied the claims and, on appeal, the Maryland Tax Court affirmed that decision. The Circuit Court for Montgomery County affirmed. The contractor appealed to the Court of Special Appeals. Before that Court considered the case, the contractor filed a petition for a writ of certiorari that we granted. We shall affirm.

The contractor contends that a state that is a party to an interstate compact may not unilaterally amend its laws to conflict with the terms of that compact. It initially points out that the express language of §10-204, Art. XVI-78 provides an exemption for the Authority from sales tax on property acquired by it to be used for a public purpose. Relying on *John McShain, Inc.* v. *Comptroller*, 202 Md. 69, 95 A.2d 473 (1953), the contractor maintains that because the Authority was entitled to an exemption from sales tax on materials that it acquired directly for the public purpose of constructing a subway, the contractor, too, was entitled to an exemption from sales tax on materials that it acquired for the Authority for that purpose. Thus, the contractor asserts, in essence, that under the terms of the

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of a private, non-profit religious, charitable, or educational organization . . . may . . . purchase the material tax-free.

* * *

E. The exemption for the purchase of building material described above applies only when the final recipient of the material is a private, non-profit religious, charitable, or educational organization . . . as described by Article 81, § 326(i), Annotated Code of Maryland. . . . [P]urchases of material which will be incorporated into the real property of the State of Maryland, including its political subdivisions, the U.S. Government, including its agencies and instrumentalities, diplomatic embassies, or credit unions, are subject to tax."

Compact, it was entitled to be exempt from a sales tax on all materials incorporated into the subway structure. The contractor concludes that the 1968 Amendment, which deprived it of its previous exemption and subjected it to a tax on materials to be incorporated into the subway structure, is in conflict with the terms of the Compact. We do not agree with this conclusion.

Section 10-204, Art. XVI-78 provides in pertinent part:

> "It is hereby declared that the creation of the Authority and the carrying out of the corporate purposes of the Authority *is* in all respects *for the benefit of the people* of the signatory states *and is for a public purpose* and that the Authority and the board will be performing an essential governmental function, including, without limitation, proprietary, governmental and other functions, in the exercise of the powers conferred by this title. *Accordingly, the Authority* and the board *shall not be required to pay taxes* or assessments *upon any of the property acquired by it* or under its jurisdiction, control, possession or supervision. . . . *This exemption shall include . . . sales tax.* . . ." (Emphasis added.)

The language of this section is plain and unambiguous. It expressly provides an exemption for the Authority from sales tax on property acquired by it to be used for a public purpose.

However, there is no express provision in the Compact granting a similar exemption to contractors from sales tax on materials acquired by them for the Authority. Indeed, there is a provision of the Compact expressly authorizing the signatory states to levy such a tax.

Section 10-203, Art. VII provides in pertinent part:

> "*Nothing herein shall be construed to amend, alter, or in any wise affect the power of the signatories* and the political subdivisions thereof *to levy and collect taxes* on the property or income of any person or company subject to this Compact or upon any material, equipment or supplies purchased by such person or companies. . . ." (Emphasis added.)

The language of this provision is clear and unambiguous. It expressly states that nothing in the Compact affects the signatory states' power to levy taxes on any material, equipment, or supplies purchased by a company subject to the Compact. In essence, this language expressly authorizes Maryland to tax contractors performing construction, repair, or alteration of real property owned by the Authority.

Here, the 1968 Amendment was an exercise of Maryland's power, retained under the Compact, to levy a sales tax on materials purchased by a contractor subject to the Compact. Because Maryland's right to levy such a tax is specifically retained under the Compact, the 1968 Amendment is not in conflict with the express provisions of §10-204, Art. XVI-78 of the Compact.

Moreover, the principles articulated in *John McShain*, 202 Md. at 72-74, 95 A.2d at 474-75, are inapplicable and do not establish that a contractor subject to the Compact is entitled to an exemption. At the time *John McShain* was decided, Art. 81, § 322 (now Art. 81, § 326) provided in pertinent part:

> "(Exemptions.) The tax hereby levied shall not apply to the following sales:
>
> (a) Sales to the State of Maryland or any of its political sub-divisions.
>
> * * *
>
> (f) Sales which are not within the taxing power of this State under the Constitution of the United States.
>
> * * *
>
> (i) Sales to any person operating a non-profit religious, charitable, scientific, literary or educational institution or organization situated in this State when such tangible personal property is purchased for use in carrying on the work of such institution or organization."

In *John McShain*, a builder contracted with the federal government (owner) to construct a building to be operated by the National Institute of Health. The federal government was

then exempt from sales tax. Art. 81, § 322(f). Nevertheless, the builder was required to pay sales tax on materials incorporated in the building. It sought a refund, claiming an exeption on the basis of the purposes of the owner's use as delineated in Art. 81, § 322(i).

Under this circumstance, the Court of Appeals did not consider an exemption based on the owner's exemption contained in Art. 81, § 322(f). Rather, it confined its consideration to an exemption based on Art. 81, § 322(i) and Rule 70[5] and held that the builder was exempt under Art. 81, § 322(i). In reaching this conclusion, the Court said:

> "The most serious objection to the allowance of the exemption is that the section, in terms, applies to sales made directly to the person operating, and not to a contractor with such person. We think, however, that it would be a strained construction to hold that persons operating the activities mentioned should be entitled to the exemption when they purchase directly from a supplier, but not when they acquire the property through an intermediary contractor. The Comptroller's regulation is very specific on the point, and while it is conceded that the Comptroller lacks the power to create an exemption beyond that granted by the statute, his interpretation is entitled to great weight as an administrative construction acquiesced in by the legislature.
>
> * * *
>
> The controlling factor upon which the exemption is based is not the instrumentality that does the purchasing, but the use of the items purchased in carrying on in Maryland the work to be promoted.
>
> * * *
>
> *The exemption* recognized in the first paragraph *depends upon the use to which the property is put, and not upon the immunity of the user, even though such immunity does not extend to its contractors under other circumstances.* Nor is it material that all activities of the federal government are considered governmental in determining the scope of its

[5] For the text of then Rule 70, see n.3.

> immunity, since *the exemption is predicated upon the use and not upon the immunity.*" *John McShain*, 202 Md. at 72-74, 95 A.2d at 474-75 (emphasis added) (citations omitted).

John McShain establishes the principle that even in the absence of an express exemption for contractors, a contractor is entitled to an exemption from sales tax on materials incorporated into a building to be used for a nonprofit religious, charitable, scientific, literary, or educational purpose as delineated in Art. 81, § 322(i). More important, it establishes the principle that the contractor's exemption depends upon the use to which the property is put and not upon the tax-exempt status of the user.

The principles articulated in *John McShain* were explicated in *Steiner Construction Co.* v. *Comptroller of Treasury*, 209 Md. 453, 458-64, 121 A.2d 838, 840-43 (1956). In *Steiner Construction*, a builder contracted with The Baltimore & Ohio Railroad Company (owner) to make alterations, improvements, or repairs to real property owned by the railroad. It was conceded that sales to railroads were then exempt from sales tax. Nevertheless, the builder was required to pay sales tax on materials incorporated into the job. The builder sought a refund claiming an exemption on the basis of the owner's exemption contained in Art. 81, § 322(f). No claim was made for an exemption based on Art. 81, § 322(i).

The Court of Appeals considered Art. 81, § 322(f), Rule 70, and the principles articulated in *John McShain* and held that the builder was not exempt under Art. 81, § 322(f). In reaching this conclusion, the Court said:

> "The appellant does argue earnestly that the reasoning of the *McShain Case* is applicable to any owner of real estate who or which is exempt from sales and use taxes, regardless of whether the exemption is founded upon sub-section (i) or some other sub-section of what is now Section 322 (formerly 261) of Article 81 of the Code (1951).
>
> As a matter of the construction of the statute we think that the *McShain Case* not only fails to support, but actu-

ally runs counter to, the appellant's contention. *If the immunity from sales and use taxes of the owner of real estate had been the criterion of the exemption of the building contractor, the* McShain Case *could easily have been decided on the basis of sub-section (f) of Section 322 (formerly 261) of Article 81. It was not so decided; on the contrary, the Court relied upon sub-section (i).* . . . This Court . . . upheld the exemption because the use involved fell within sub-section (i), saying, 'We think it is quite immaterial that the activity is conducted by a federal agency, rather than by a private agency or by the State.' Later the Court added, 'The exemption recognized in the first paragraph [of Rule 70] depends upon the use to which the property is put, and not upon the immunity of the user, even though such immunity does not extend to its contractors under other circumstances.'

In the instant case there is no use comparable to that involved in the McShain Case. *The exemption relied upon by the appellant is contained in Section 261, paragraph (f)* of Article 81 of the 1947 Supplement to the 1939 Code [1951 Edition, Article 81, Section 322 (f)]. It covers 'Sales which are not within the taxing powers of this State under the Constitution of the United States.' This is no more than an express recognition of the inescapable; it manifests no legislative intent to further the activities of the beneficiaries of this unavoidable exemption. Consequently, there is no such foundation as in the case of charitable or educational institutions for deducing a legislative intent which would support a broad interpretation of the exemption. Likewise, there is no such consideration as might prompt the State to exempt itself or its political subdivisions from paying State taxes.

* * *

The *McShain Case* recognized an exemption which the General Assembly thought it wise to grant. *It might be perfectly logical to carry back realty owners' exemptions to contractors in all cases, but this has not been done, as the* McShain Case *itself shows.* A contention somewhat similar to that of the present appellant along this line was advanced but rejected in *Comptroller* v. *Joseph F. Hughes & Co., Inc.*, 209 Md. 141, 120 A.2d 343, in which the opinion was filed on the same day that the instant case was argued. In that case contractors doing work for the City of

Baltimore and other political sub-divisions of the State of Maryland sought exemption from sales and use taxes on items of personal property purchased to fulfill their contracts with various municipalities, which were consumed in the work and were not incorporated in the finished product. The Court, again speaking through Judge Henderson, there said:

'The appellee argues that the legislative purpose in exempting sales to the State and its political sub-divisions, as well as to charitable and other institutions of the types mentioned, was to enable them to obtain buildings and other property used in their governmental capacity, or for the furtherance of their charitable purposes, at a lower cost, and that purpose would be served by the exemption of expendible items as well as of items that survive the completion of the structures. This may be true, but in construing tax statutes the courts do not now attach much weight to arguments based on the economic incidence of the tax. That same argument might be made as to items which go into the contractor's inventory as a part of his capital assets or equipment, and suffer deterioration and depreciation during the progress of the work. In any event it is a matter of legislative policy as to where the line should be drawn.'" *Steiner Construction,* 209 Md. at 460-64, 121 A.2d at 840-43 (emphasis added) (citation omitted).

Steiner Construction establishes that the principles articulated in *John McShain* are limited in application to claims made on the basis of the purpose of the owner's use as delineated in Art. 81, § 322(i) and not on the basis of the owner's exemption under other sections such as Art. 81, § 322(f).

Here the contractor claims an exemption based on §10-204, Art. XVI-78 of the Compact which provides that because the Authority was created for a public purpose, it should not be required to pay taxes on property acquired by it. It is, therefore, unclear whether in analogizing to *John McShain* the contractor claims an exemption on the basis of the Authority's tax-exempt status or on the basis of the purpose of the use.

However, the contractor's contention that it is the 1968 Amendment to Art. 81, § 326(a) which deprives it of tax-ex-

empt status makes it plain that in analogizing this case to *John McShain*, the contractor's claim is based on the Authority's tax-exempt status under Art. 81, § 326(a) (formerly Art. 81, § 322(a)) rather than the purpose of the use as delineated in Art. 81, § 326(i) (formerly Art. 81, § 322(i)). Under these circumstances, the principles of *John McShain* do not apply. *Steiner Construction*, 209 Md. at 460-62, 121 A.2d at 841.

This case cannot be analogized to *John McShain* for yet another reason. Article 81, § 322 (now Art. 81, § 326), the section of the Retail Sales Act construed in *John McShain*, contained no express provision concerning the tax status of contractors performing construction, repair, or alteration of real property for the State of Maryland. Here a section of the Compact, §10-204, Art. XVI-78, is being construed. The Compact, however, contains an express provision, §10-203, Art. VII, which, as set forth above, authorizes Maryland to tax contractors performing such work for the Authority. For this reason, too, the principles of *John McShain* do not apply.

Finally, even if the principles of *John McShain* were applicable, the contractor here would not be entitled to an exemption. Maryland is expressly authorized by the plain language of §10-203, Art. VII of the Compact to amend its laws unilaterally in order to tax contractors performing work for the Authority. Therefore, even if, at the time of the adoption of the Compact in 1965, §10-204, Art. XVI-78 provided a tax exemption for a contractor subject to the Compact, Maryland would, nonetheless, have the authority under §10-203, Art. VII subsequently abolish that exemption.

In sum, it is immaterial whether the principles of *John McShain* are applicable. Because Maryland is expressly authorized by the plain language of §10-203, Art. VII of the Compact to tax contractors performing construction, repair, or alteration of real property owned by the Authority, the 1968 Amendment to Art. 81, § 326(a) which imposed such a

tax is not in conflict with the Compact.[6] The contractor is not entitled to a sales tax refund.[7] Accordingly, we shall affirm.

JUDGMENT AFFIRMED.
COSTS TO BE PAID BY PETITIONER.

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[6] Delaware River & Bay Auth. v. Carello, 43 Del.Ch. 213, ____, 222 A.2d 794, 799 (1966), relied on by the contractor is inapposite. There, unlike here, a unilaterally enacted statute was in conflict with an express provision of a Compact.

[7] In view of this decision, we need not consider the contractor's contention that, in determining whether the contractor is entitled to a refund, it is immaterial whether the contractor "bore the burden of the tax or shifted it to others."

APPENDIX B

IN THE CIRCUIT COURT FOR MONTGOMERY COUNTY, MARYLAND

Law No. 51375

JAMES MCHUGH CONSTRUCTION COMPANY

Appellant

v.

COMPTROLLER OF THE TREASURY,

Appellee

Opinion And Order

FILED
MARCH 11, 1980

Appellant, the James McHugh Construction Company, appeals a decision of the Maryland Tax Court reaffirming a denial by the Comptroller of the Treasury of a refund of certain sales and use taxes paid by the Appellant.

The essential facts in this case are not in dispute and are restated here from the briefs of the respective parties. On October 1, 1974, the Appellant entered into a contract with the Washington Metropolitan Transit Authority (hereafter, "WMATA") (Contract No. 1A0101) to construct a portion of the Washington Metropolitan Area subway system. The portion to be constructed is designated Section A-10a, the Rockville Route Tunnels, which is located beneath Wisconsin Avenue in Chevy Chase and Bethesda, Maryland, extending northward from the District of Columbia line.

The McHugh-WMATA contract was entered into in accordance with the provisions of the Washington Metropolitan Area Transit Authority Compact (the "Compact"), an Interstate Compact entered into by the State of Maryland, the Commonwealth of Virginia, and the District of Columbia. The Compact was signed by each party and was consented to by the Congress in accordance with Article I, Section 10,

Clause 3 of the United States Constitution (Public Law 89-774, 80 Stat. 1324). The State of Maryland enacted the Compact by Ch. 869, Laws of Maryland (1965), now codified in section 10-24, Transportation Article, Annotated Code of Maryland (1977 vol. and 1979 Cum. Supp.).

The sales and use taxes paid by the Appellant, for which refund is sought, were paid on materials purchased by it for the performance of the McHugh-WMATA contract and such materials have been physically incorporated into and remain a part of the finished contract job.

At the time the Compact was enacted by Maryland and the other parties thereto and at the time the Compact was consented to by the Congress, the Maryland Sales Tax Law provided that contractors performing jobs for the State of Maryland or any of its political subdivisions were not required to pay sales or use taxes on materials or supplies which would be incorporated into the job. Subsequently, after the adoption of the Compact, but some six years before Appellant entered into its contract with WMATA, Maryland amended its sales tax law so as to impose the tax on contractors purchasing materials pursuant to contracts for the construction, alteration, or repair of real property entered into with the State of its subdivisions.

During the time of the McHugh-WMATA contract, Appellant has paid the sales and use taxes but has duly and timely filed claims with the Comptroiler of the Treasury seeking refunds on the amounts paid. The Comptroller denied claims for refunds and the Appellant appealed to the Maryland Tax Court. From an order of the Maryland Tax Court affirming the decision of the Comptroller of the Treasury, the Appellant appeals. For the reasons set forth below, the Court affirms the decision of the Maryland Tax Court.

Appellant's argument is that the Compact prohibits the imposition by the signatory parties of a sales and use tax on contractors for the purchase of personal property to be incorporated into the job. In principal support of this argument,

Appellant cites paragraph 78 of the Compact which says, in pertinent part, that "the Authority and the Board shall not be required to pay taxes or assessments on any of the property acquired by it or under its jurisdiction, control, possession, or supervision. . . ." Appellant further argues that this language should be construed to exempt contractors from payment of taxes on material for the job. Reliance is placed first on the proposition that imposition of the tax in these circumstances illegally burdens the Compact, and second on the rationale of the decision in *John McShain, Inc.* v. *Comptroller*, 202 Md. 68 (1953). This Court is of the opinion that although the *McShain* opinion might have dictated a different result, its force in the present case is nullified by the subsequent amendment by the legislature of Chapter 452, Section 5, Acts of 1968, now codified at Section 326(a), Transportation Article, Annotated Code of Maryland (1975 vol. and 1979 Cum. Supp.). Section 326(a) states that the retail sales tax shall not be levied on sales to the State of Maryland, "[p]rovided that this subsection shall not be construed or applied to exempt any sale . . . of tangible personal property to contractors or builders to be used for the construction, repair or alteration of real property. . . ."

The Court is of the further opinion that Section 326(a) does not impose an illegal burden on the Compact, because Article VII of the Compact states:

> Nothing herein shall be construed to amend, alter, or in any wise affect the power of the signatories and the political subdivisions thereof to levy and collect taxes on the property or income of any person or company subject to this Compact or upon any material, equipment or supplies purchased by such person or companies or to levy, assess and collect franchise or other similar taxes, or fees for the licensing of vehicles and the operation thereof.

Review by the Circuit Court of decisions of the Maryland Tax Court is governed by Section 229(1)-(o), Transportation Article, Annotated Code of Maryland (1975 vol. and 1979 Cum. Supp.), wherein it is stated that the Circuit Court "shall affirm the Tax Court order if it is not erroneous as a matter of

law and if it is supported by substantial evidence appearing in the record." Upon consideration of the issues raised in this appeal, and of the decision of the Maryland Tax Court, it is therefore

ORDERED this 10th day of March, 1980, that the appeal of James McHugh Construction Company be, and the same is hereby, dismissed.

/s/ STANLEY B. FROSH
Stanley B. Frosh
Judge of the Circuit Court
Montgomery County, Maryland

APPENDIX C

IN THE MARYLAND TAX COURT

Sales Tax No. 66

JAMES MCHUGH CONSTRUCTION COMPANY

v.

COMPTROLLER OF THE TREASURY,

Memorandum Of Grounds For Decision

Petitioner, Jame McHugh Construction Co., comes before this Court seeking a reversal of a final determination by the Comptroller that denies a refund of sales and use taxes.

In 1965, Maryland entered into an Interstate Compact with Virginia and the District of Columbia that created the Washington Metropolitan Area Transit Authority (Metro). See Ann. Code Md., Transportation Article (1977), Sections 10-201-204 (1978 Cum. Supp.). The Compact was ratified by the Congress of the United States on November 6, 1966, Public Law 89-774, 80 Stat. 1324.

In 1968, Maryland amended its sales and use tax exemption statute, by Chapter 452 Section 5, Acts of 1968 (The Act), now codified at Ann. Code Md., Article 81 (1975 Replacement Volume), Section 326(a). Prior to this amendment, Section 326(a) had been judicially construed as extending an exemption from sales taxes to purchases of supplies made by contractors doing business with the State, *John McShain, Inc.* v. *Comptroller,* 202 Md. 68, 95 A.2d 473 (1953).

In 1974, Petitioner entered into a contract with Metro to build a portion of the Metro Subway System. Petitioner paid sales and use taxes on supplies purchased in performance of that contract and now seeks a refund of those taxes.

Petitioner does not attack the validity of the Act on its fact, but denies the applicability of the Act to itself. First, it con-

tends that Maryland's ratification of the Compact precluded it from amending its Sales Tax Law so as to deny exemptions to contractors with Metro. This argument is based on the accepted proposition that parties to an Interstate Compact may not unilaterally enact laws that burden that Compact. *West Virginia* v. *Sims*, 341 U.S. 22, 28, 95 L.Ed. 713, 722, 71 S.Ct. 557, 560 (1951); *Delaware River and Bay Authority* v. *Carello*, 222 A.2d 794, 798, 43 D.Ch. 213 (1966). The issue is whether the Act, as applied to contractors with Metro, is such a forbidden burden. Petitioner claims that it is because the effect of taxing a contractor with Metro is "necessarily to increase the cost of construction, thereby actually hindering construction of the (Metro) subway system . . ." (Pet. Br., p. 16).

Assuming, for the moment, that Petitioner's conclusion is true, it is still unclear whether such an increase in cost, caused by the State's recission of sales tax exemption, creates the type of burden that is forbidden. No cases on point have been presented to us, nor can we find any. Petitioner draws an analogy to the facts of *Carello, supra*, where the Delaware Supreme Court struck down a post-Compact statute authorizing collective bargaining as an impermissible burden on that Compact. However, that case sheds little light on the question of whether the indirect effect of a tax law can constitute such a burden, and, if so, how much of an increased cost must be shown?

We need not reach these legal questions for we find, as a matter of fact, that the Act has not burdened the Compact in the manner Petitioner has claimed. Petitioner claims that the cost of Metro must "necessarily" be increased because contractors like itself *must* add the cost of the sales tax to its final bill. However, there is no showing that contractors have passed on costs to such an extent as to burden Metro, in fact there is no showing that contractors have passed on any costs resultant from the Act. Furthermore Petitioner itself did not include the cost of the sales tax in its initial cost estimate in 1974 — even though the Act had been effective for six years. We cannot conclude that the Act "necessarily" increased the

cost of Metro, in that Petitioner's own actions of absorbing the cost of the sales taxes, belie that contention.

Petitioner's second argument is that the Compact itself prohibits imposition of sales or use taxes upon contractors with Metro. Petitioner cites paragraph 78 of Article XII of the Compact, which provides:

> "It is hereby declared that the creation of the Authority and the carrying out of the corporate purposes of the Authority is in all respects for the benefit of the people of the signatory states and is for a public purpose and that the Authority and the board will be performing an essential governmental function, including, without limitation, proprietary, governmental and other functions, in the exercise of the powers conferred by this title. Accordingly, the Authority and the board shall not be required to pay taxes or assessments upon any of the property acquired by it or under its jurisdiction, control, possession or supervision or upon its activities in the operation and maintenance of any transit facilities or upon any revenues therefrom and the property and income derived therefrom shall be exempt from all federal, state, District of Columbia, municipal and local taxation. This exemption shall include, without limitation, all motor vehicle license fees, sales taxes and motor fuel taxes."

Petitioner argues that a liberal construction of paragraph 78 indicates that the signatories intended that they surrender any taxing authority that could ultimately cause the cost of Metro to be raised.

There are two short answers to this argument. First, no construction at all of paragraph 78 is needed because it is not ambiguous, *Chillum-Adelphi Volunteer Fire Department, Inc.* v. *Prince George's County*, 269 Md. 486, 491, 307 A.2d 481, 484 (1973), and clearly exempts only Metro, not any of its contractors, from taxation. Second, an opposite intention of the signatories regarding surrendering their taxing authority is revealed by Article VII of the Compact:

> "Nothing herein shall be construed to amend, alter, or in any wise affect the power of the signatories and the po-

litical subdivisions thereof to levy and collect taxes on the property or income of any person or company subject to this Compact or upon any material, equipment or supplies purchased by such person or companies or to levy, assess and collect franchise or other similar taxes, or fees for the licensing of vehicles and the operation thereof."

Accordingly, we shall pass an order affirming the decision of the Comptroller in this case.

APPENDIX D

BEFORE THE
COMPTROLLER OF THE TREASURY
RETAIL SALES TAX DIVISION

IN THE MATTER OF

JAMES MCHUGH CONSTRUCTION COMPANY
2222 South Indiana Avenue
Chicago, Illinois 60616

Opinion

This Opinion is the result of a formal hearing held on December 2, 1975, in the Office of the Comptroller at the State Office Building in Baltimore, Maryland, and supporting memoranda subsequently filed by both McHugh Construction Company (hereinafter referred to as "McHugh" or "taxpayer") and counsel for the Comptroller. The hearing was requested by McHugh to secure the refund of sales and use taxes paid on materials and supplies used by it in the construction of a portion of the Washington Metropolitan Area subway system located in Montgomery County just north of the District of Columbia line. The amount in controversy was the subject of three applications for refund, the first dated August, 6, 1975 in the amount of $3,097.21, the second dated August 27, 1975 in the amount of $3,921.13, and the third dated September 22, 1975 in the amount of $874.88. It has been stipulated by the parties that such amounts shall be presumed to be correct, subject to subsequent audit.

On October 1, 1974, McHugh entered into a contract with the Washington Metropolitan Area Transit Authority ("WMATA") (Contract No. 1A0101) to construct a portion of the Washington Metropolitan Area subway system. All but several hundred of approximately 18,000 linear feet of single-trade tunnel line which the contract calls for are to be constructed beneath Wisconsin Avenue in Chevy Chase and Bethesda, Maryland; the remainder will be located just south of the Maryland boundary in the District of Columbia.

The McHugh-WMATA contract was entered into in accordance with provisions of the Washington Metropolitan Area Transit Authority Compact (the "Compact"), an Interstate Compact entered into by the State of Maryland, the Commonwealth of Virginia, and the District of Columbia, and duly consented to by the Congress in accordance with Article I, Section 10, clause 3, of the Constitution of the United States.

The Compact was enacted by the State of Maryland by Ch. 869, Laws of Maryland (1965), Annotated Code of Maryland (1971 Repl. Vol. and 1975 Cum. Supp.), Article 41, Sections 317-1 *et seq.;* by Virginia in 1966 (c. 2, Acts 1966); and it was enacted by Congress on behalf of the District of Columbia, and consented to by that body on November 6, 1966 (Pub. L. 89-774, 80 Stat. 1324). By the terms of the Compact, the States of Maryland and Virginia and the District of Columbia are each signatory parties to the Compact and are each bound thereby.

At the time the Compact was enacted, the Maryland sales tax law granted to contractors performing jobs for the State of Maryland or any of its political subdivisions an exemption from sales or use taxation on materials or supplies which would be incorporated into real property. In 1968, after the adoption of the Compact and the congressional consent thereto, Maryland amended its sales tax law so as to revoke the exemption granted to contractors performing construction contracts for the State or its political subdivisions. Ch. 452, Laws of Maryland (1968).

The refund requests represent the sales and use taxes imposed under the Maryland sales tax law as amended in 1968 upon materials purchased by McHugh which are or will be incorporated into real property. The ability of the State of Maryland, as a signatory of the Compact, to impose such taxes on a contractor performing a construction contract for the WMATA (an instrumentality and agency of the State of Maryland) is the issue upon which the instant controversy is based.

The WMATA Compact provides in pertinent part:

WASHINGTON METROPOLITAN AREA TRANSIT AUTHORITY

4. There is hereby created, as an instrumentality and agency of each of the signatory parties hereto, the Washington Metropolitan Area Transit Authority which shall be a body corporate and politic, and which shall have the powers and duties granted herein and such additional powers as may hereafter be conferred upon it pursuant to law.

ARTICLE IV

PLEDGE OF COOPERATION

11. Each Signatory pledges to each other faithful cooperation in the achievement of the purposes and objects of this Title.

TAX EXEMPTION

78. It is hereby declared that the creation of the Authority and the carrying out of the corporate purposes of the Authority is in all respects for the benefit of the people of the signatory states and is for a public purpose and that the Authority and the board will be performing an essential governmental function, including, without limitation, proprietary, governmental and other functions, in the exercise of the powers conferred by this title. Accordingly, the Authority and the board shall not be required to pay taxes or assessments upon any of the property acquired by it or under its jurisdiction, control, possession or supervision or upon its activities in the operation and maintenance of any transit facilities or upon any revenues therefrom and the property and income derived therefrom shall be exempt from all federal, state, District of Columbia, municipal and local taxation. This exemption shall include, without limitation, all motor vehicle license fees, sales taxes and motor fuel taxes.

I.

Taxpayer reads Section 78 of the Compact itself as prohibiting Maryland from imposing sales or use taxes upon McHugh. Stressing the "essential governmental function" of the WMATA and the benefit to be conferred upon the people of the signatory states by the carrying out of the WMATA's purposes, McHugh argues that without the exemption granted to the WMATA, one would have the anomaly "of a State's paying its share of the project cost with one hand, and with the other hand, collecting its sales tax on the personal property being incorporated into that project." By extrapolating taxpayer's argument, one is led to the conclusion that by imposing the tax upon McHugh the anomaly is complete — "a State enriching itself by collecting taxes from those who are performing important governmental and public functions for which the State itself, as well as the other contracting parties to the Compact, is paying." Memorandum in Support of Applications for Refund, p. 15.

Taxpayer goes on at some length to support the proposition that the Compact is entitled to a liberal construction so as to effectuate its purposes. The proposition seems undisputed, since it can be found within the provisions of the Compact itself. Section 85 of the Compact, Annotated Code of Maryland, Article 41, Section 317-85, reads, in pertinent part, as follows:

> "It is the legislative intent that the provisions of this title be reasonably and liberally construed."

Having established that the Compact is entitled to a liberal construction, McHugh argues that because the tax will necessarily result in higher contract prices to WMATA, it therefore directly burdens the Compact and the effectuation of its purposes. In view of the expansive interpretation the agreement should be given, it is argued that the tax is imposed in contravention of the provision of the Compact granting the Authority tax exempt status (see paragraph 78, *supra*). The argument of McHugh assumes that a court would be free to ap-

ply the principles of statutory construction set forth in Section 85. It is, however, well settled that the rules of statutory construction are resorted to only when the provisions of a statute are ambiguous (i.e., equally susceptible to two reasonable interpretations). The courts may not under the guise of construction supply omissions or remedy possible defects in a statute, or insert exceptions not made by the Legislature. *State* v. *Zitomer*, 275 Md. 534 (1975); *Purifoy* v. *Mercantile-Safe Deposit & Trust Co.*, 273 Md. 58 (1974); *Gatewood* v. *State*, 244 Md. 609 (1966).

The language of Section 78 leaves no room for interpretation. It is only the Authority and the Board which are not required to pay the taxes or assessments specified; no provision is made for exemption from taxation of any other person. Taxing power is never presumed to be relinquished by the state unless such an intention is expressed in clear and unambiguous language. *Celanese Corporation of America* v. *Davis*, 186 Md. 463 (1946).

Moreover, to embrace the expansive interpretation advocated by McHugh is to invite an endless host of interpretive difficulties. In its reply memorandum, taxpayer proposes to draw the distinction between "direct" and "indirect" burdens placed on the Compact. For example, a tax on McHugh's corporate profits by Maryland would include innumerable elements that go into the determination of McHugh's Maryland income tax liability in addition to profits or losses by McHugh on the Metro subway job. Accordingly, this tax would only "indirectly" burden the Compact and would be permissible. "By contrast, every cent of sales or use tax exacted from McHugh is directly attributable to the purchase of materials being incorporated into the Rockville Route Tunnels under the interstate Compact, and imposes a direct burden on the Compact and the effectuation of its purposes." Reply Memorandum in Support of Applications for Refund, p. 3.

We have difficulty discerning, however, where McHugh's "direct burden" chain would end. Presumably the supplier from whom McHugh purchases the materials it uses in the

construction contract could also claim the same exemption under the identical theory. Every cent of sales or use tax exacted from the supplier would be directly attributable to the purchase of materials incorporated into the Rockville Route Tunnels. Everyone's costs would rise; the Compact would be "directly burdened." And what of the supplier's supplier? Having forged the first link in a causal chain of cost escalation, taxpayer would set us on a course which ultimately would obliterate the distinction he proposes to establish. The line between direct and indirect burdens on the Compact has been clearly and wisely drawn by the legislators in the express terms of Section 78, and we see no sound reason to extend it further.

II.

Taxpayer further argues that, since the Maryland sales tax law in effect at the time of the Compact's creation and promulgation by the parties and Congress was "one of the existing facts underlying the Compact," Maryland could not unilaterally amend its laws to impose sales and use taxes with respect to materials to be incorporated into the job. By negating one of the bases upon which the Compact was entered into, McHugh argues, Maryland has unreasonably burdened the WMATA and its contractors in carrying out the public purposes for which the Compact was adopted. As the taxes imposed upon McHugh would eventually be borne by the WMATA, McHugh contends that the action of the Comptroller breaches Section 11 of the Compact, in which each party pledged to the others "faithful cooperation in the achievement of the purposes and objects" of the Compact.

We find ourselves, however, unable to accept the basic premise upon which McHugh's argument rests, i.e., that the provisions of the Maryland sales tax law as in effect in 1965-66 was one of the bases upon which the parties entered into the Compact. McHugh has presented no evidence that such an exemption for purchases by contractors with the State of Maryland and its political subdivisions was any part of the con-

sideration received by the District of Columbia or the Commonwealth of Virginia in connection with their adoption of the Compact. A reading of Section 78 of the Compact reveals no exemption created for contractors of the WMATA, though various other provisions refer to the ability of the Authority to contract and the methods of compensating contractors. Absent an express demonstration of reliance by the parties on the continuation of the tax exemption, it cannot be presumed to exist. The imposition of a new tax is one of the usual hazards of business and seldom, if ever, impairs the obligation of a pre-existing contract. *McShain* v. *District of Columbia*, 205 F.2d 882 (D.C. Cir. 1953). In that case, a contractor with the District of Columbia was not absolved of a duty to pay tax on personal property purchased subsequent to passage of the District of Columbia Sales Tax Act on contracts formed prior to passage of the Act. Even were McHugh able to present evidence to support its position of reliance by the parties, the contract between the states and the District of Columbia is unambiguous and the parol evidence rule would operate to exclude any evidence which would tend to vary or contradict the written agreement.

Having failed to find merit in either of McHugh's theories, its request for refund is accordingly denied.

/s/ BERNARD F. MOAN
Bernard F. Moan
Hearing Officer

July 23, 1976

Opposition

Office - Supreme Court, U.S.
FILED
NOV 18 1981
ALEXANDER L. STEVAS,
CLERK

No. 81-713

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

JAMES McHUGH CONSTRUCTION COMPANY,
Petitioner,

v.

COMPTROLLER OF THE TREASURY, RETAIL SALES TAX DIVISION, FOR THE STATE OF MARYLAND,
Respondent.

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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The Daily Record Co., Baltimore, MD 21202

QUESTION PRESENTED

Did the lower court properly hold that the express language of the Washington Metropolitan Area Transit Authority (WMATA) Compact authorized the State of Maryland to amend its laws after the Compact was signed, to impose a sales tax on purchases of materials by real property contractors doing work for WMATA or other political subdivisions?

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The question presented for review is simply one of construction of the plain and unambiguous terms of an interstate compact, which warrants no review by this Court because it is neither novel nor in conflict with another court's decision, but was correctly decided by the lower court in accordance with the decisions of this Court.	5
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No. 81-713

IN THE

Supreme Court of the United States

OCTOBER TERM, 1981

JAMES McHUGH CONSTRUCTION COMPANY,
Petitioner,

v.

COMPTROLLER OF THE TREASURY, RETAIL SALES TAX DIVISION, FOR THE STATE OF MARYLAND,
Respondent.

ON WRIT OF CERTIORARI TO THE COURT OF APPEALS OF MARYLAND

BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

STATEMENT OF THE CASE

On September 15, 1960, Congress, on behalf of the State of Maryland, the Commonwealth of Virginia and the District of Columbia consented to the Washington Area Transit Regulation Compact (WATRC). Pub. L. No. 86-794, 74 Stat. 1031, as amended by Pub. L. No. 87-767, 76 Stat. 674. The Compact established a common agency intended to alleviate transit and traffic problems in the Washington D.C. metropolitan area. The text of the Compact was codified by Maryland in 1959 as Art. 41, Section 268 through Section 317, Md. Anno. Code and

subsequently recodified as Section 10-203 of the Transportation Article of the Maryland Code.

In 1965, Maryland and the other jurisdictions adopted an amendment to WATRC known as the Washington Metropolitan Area Transit Authority (WMATA) Compact. The WMATA Compact is Title III of WATRC and was consented to by Congress on November 6, 1966. Pub. L. No. 89-744, 80 Stat. 1324. The WMATA Compact was originally codified by Maryland as Art. 41, Section 317-1 through 317-86 of the Md. Anno. Code and subsequently recodified as Section 10-204 of the Transportation Article of the Maryland Code. WMATA, an independent public agency, was created to plan, develop, finance, and operate improved transit facilities in the Washington metropolitan area.

Approximately three years after the WMATA Compact was enacted by Maryland, the Maryland General Assembly amended Art. 81, Section 326(a), Md. Code, to provide that a contractor that performs a real property contract for the State or its political subdivisions shall not be exempt from sales tax on its purchases of materials in fulfilling the contract. Chapter 452, *Laws of Maryland* (1968). Prior to 1968, and including the period during which the Compact was adopted, purchases of such materials were not subject to sales and use tax.

On October 1, 1974, approximately six years *after* the amendment to the Maryland sales tax law, McHugh Construction Company (McHugh) entered into a contract with WMATA (Contract No. 1A0101) for McHugh to build a portion of the Rockville Route Tunnels, from the District of Columbia line northward into Maryland. McHugh paid sales tax on materials it purchased and physically incorporated into the project. It is the payment of these taxes that McHugh claims should be refunded by Maryland.

In August and September, 1975, McHugh filed with the Comptroller of the Treasury three claims for refund of sales and use taxes paid by it on its purchase of materials to construct the Rockville Route Tunnels for WMATA. After an administrative hearing, in a opinion filed July 23, 1976, the Comptroller denied McHugh's claim.

McHugh appealed the Comptroller's determination to the Maryland Tax Court on August 9, 1976. McHugh raised two principal arguments: (1) that Maryland illegally burdened the Compact by amending its sales tax law after the Compact was enacted, and (2) paragraph 78 of the Compact expressly exempted McHugh from paying sales tax. Following a *de novo* proceeding, in a Memorandum of Grounds for Decision dated February 23, 1979, the Tax Court affirmed the Comptroller's decision in denying the claim for refund by deciding that (1) there was no need to reach McHugh's first issue on a legal basis because McHugh failed to prove factually that WMATA was burdened (A. 18a) and (2) that McHugh's second argument was without merit because the clear language of paragraph 78 only exempted the Authority and its Board from paying tax and not contractors doing work for the Authority and the Board. The Court also decided that the WATRC Compact expressly authorized the parties to the Compact to tax contractors doing work for WMATA (A. 19a-20a).

On March 21, 1979, McHugh appealed to the Circuit Court for Montgomery County, Maryland. In a written opinion and order dated March 11, 1980, Judge Stanley Frosh affirmed the decision of the Tax Court (A. 13a-16a).

McHugh appealed Judge Frosh's order to the Court of Special Appeals of Maryland on April 9, 1980, and on August 15, 1980, filed a Petition for Writ of Certiorari in the Court of Appeals of Maryland. On September 9, 1980,

before briefing in the Court of Special Appeals, the Court of Appeals granted the Petition.

McHugh argued essentially three points to the Court of Appeals: (1) Maryland exceeded its authority in levying the tax on McHugh as a contractor doing work for WMATA, (2) the express language of paragraph 78 exempted McHugh from paying sales tax, a proposition McHugh claimed was supported by *John McShain, Inc. v. Comptroller,* 202 Md. 69, 95 A.2d 473 (1953), and (3) it was irrelevant factually whether the taxes paid by McHugh actually burdened the Compact. Answering McHugh's second point first, the Court of Appeals held in an opinion filed July 17, 1981 that (1) paragraph 78 of the Compact did not exempt McHugh from tax, the *John McShain* case was inapposite, and to the contrary, Art. VII of WATRC expressly authorized taxation of contractors doing work for WMATA (A. 5a-6a), (2) that in light of its initial determination that the Compact authorized taxation of McHugh, Maryland did not exceed its authority (A. 12a, n.6), and (3) it was not necessary to decide whether WMATA bore the burden of the tax (A. 12a, n.7).

A Petition for Writ of Certiorari was docketed by McHugh in this Court on October 14, 1981.

SUMMARY OF THE ARGUMENT

The questions presented by McHugh in its Petition would not be reached by the Court if it grants certiorari. The only question the court would review, regardless of its disposition of the case, would be whether the express terms of the Compact allowed Maryland to levy a sales tax on contractors doing work for WMATA. Construction of the plain words of a document does not merit Supreme Court review, particularly when, as in this case, it was construed properly by the three lower courts.

Since the Petition presents nothing novel for review and the question was decided correctly by the lower courts, certiorari should be denied.

ARGUMENT

THE QUESTION PRESENTED FOR REVIEW IS SIMPLY ONE OF CONSTRUCTION OF THE PLAIN AND UNAMBIGUOUS TERMS OF AN INTERSTATE COMPACT, WHICH WARRANTS NO REVIEW BY THIS COURT BECAUSE IT IS NEITHER NOVEL NOR IN CONFLICT WITH ANOTHER COURT'S DECISION, BUT WAS CORRECTLY DECIDED BY THE LOWER COURT IN ACCORDANCE WITH THE DECISIONS OF THIS COURT.

The key issue that controlled the disposition of this case in the lower courts was whether the language of the Compact allowed Maryland to levy a sales tax on McHugh's purchases of materials for the Rockville Route Tunnels contract with WMATA. The lower court's affirmative answer to this issue made it unnecessary to rule on other questions presented by McHugh.

This Court is similarly being asked simply to construe the language of the Compact. The questions presented by McHugh in its Petition for Writ of Certiorari are derivative of this issue. If the Court decides as the lower courts did, that the terms of the Compact permitted the tax to be levied on McHugh, Maryland obviously would be permitted to unilaterally amend its sales tax law (Question 1, Petition for Writ of Certiorari, at i). Since Maryland could amend its sales tax law, there would be no impairment of the State's contract obligation, nor would there be any infringement of McHugh's title, rights, privileges and immunities. (Questions 2 and 3, Petition for Writ of Certiorari at i). If the Court decides that the language of the Compact prohibited the imposition of the tax on McHugh it would be unnecessary to determine whether the issues framed within the questions presented also

prohibited the imposition of the tax.[1] Consequently, the Court is presented with no novel question of law for determination, but rather, the routine construction of the language of a document. It is submitted that this question does not merit review by this Court.[2]

Review by this Court is unnecessary because the Court of Appeals of Maryland correctly decided the question presented. McHugh contends in its Petition that paragraph 78 of the Compact exempted McHugh from payment of sales tax. The Court of Appeals correctly rejected this argument as follows:

> "Section 10-204, Art. XVI-78 provides in pertinent part:
>
> > 'It is hereby declared that the creation of the Authority and the carrying out of the corporate purposes of the Authority is in all respects *for the benefit of the people* of the signatory states *and is for a public purpose* and that the Authority and the board will be performing an essential governmental function, including, without limita-

[1] Although a ruling by the Court that the Compact prohibits the taxation of McHugh forecloses the necessity of also ruling on the questions presented by the Petitioner, other arguments raised by Maryland would have to be addressed. Specifically, one question is whether McHugh proved as a matter of fact its payment of sales tax actually burdened WMATA, and if it did not prove it, whether McHugh in any event is entitled to relief.

[2] Even if the questions presented by McHugh somehow could be addressed, two of them should not be reviewed because they were not briefed or argued by McHugh in the Court of Appeals. Specifically, McHugh did not argue whether unilateral amendment of the Maryland sales tax law impaired the State's contract obligation as a party to the Compact, and it did not argue that its title, rights, privileges and immunities under the U.S. Constitution were impaired, although this issue was raised in the Maryland Tax Court. Issues not raised and decided below ordinarily will not be reviewed by the Supreme Court. *United States v. Ortiz*, 422 U.S. 891, 45 L. Ed. 2d 623, 95 S. Ct. 2585 (1975), *Ramsey v. United Mine Workers*, 401 U.S. 302, 28 L. Ed. 2d 64, 91 S. Ct. 658 (1971).

> tion, proprietary, governmental and other functions, in the exercise of the powers conferred by this title. *Accordingly, the Authority* and the board *shall not be required to pay taxes* or assessments *upon any of the property acquired by it* or under its jurisdiction, control, possession or supervision. . . . *This exemption shall include . . . sales tax . . .*' (Emphasis added).

The language of this section is plain and unambiguous. It expressly provides an exemption for the Authority from sales tax on property acquired by it to be used for a public purpose.

"However, there is no express provision in the Compact granting a similar exemption to contractors from sales tax on materials acquired by them for the Authority. Indeed, there is a provision of the Compact expressly authorizing the signatory states to levy such a tax.

"Section 10-203, Art. VII provides in pertinent part:

> *'Nothing herein shall be construed to amend, alter, or in any wise affect the power of the signatories* and the political subdivisions thereof to *levy and collect taxes* on the property or income of any person or company subject to this Compact or upon any material, equipment or supplies purchased by such person or companies. . . .' (Emphasis added).

The language of this provision is clear and unambiguous. It expressly states that nothing in the Compact affects the signatory states' power to levy taxes on any material, equipment, or supplies purchased by a company subject to the Compact. In essence, this language expressly authorizes Maryland to tax contractors performing construction, repair, or alteration of real property owned by the Authority.

"Here, the 1968 Amendment was an exercise of Maryland's power, retained under the Compact, to levy a sales tax on materials purchased by a contractor subject to the Compact. Because Maryland's right to levy such a tax is specifically retained under the

> Compact, the 1968 Amendment is not in conflict with the express provisions of Section 10-204, Art. XVI-78 of the Compact." (A. 5a-6a).

McHugh argues at page 8 of its Petition that the Court of Appeals misconstrued Art. VII, Section 10-203. McHugh would limit its plain meaning to only those taxes that were imposed at the time the Compact was enacted. There is no language in the section to support such a construction, and it would require the judicial insertion of a provision that does not exist into the language of a plain and unambiguous section.

McHugh's reliance on *John McShain, Inc. v. Comptroller,* 202 Md. 69, 95 A.2d 473 (1953) is misplaced for the variety of reasons stated in the Court of Appeals opinion (A. 6a-11a). Also, once it is concluded that the Compact authorizes the imposition of a sales tax on McHugh, the construction of the *McShain* case presents no federal question for review.

The case upon which Petitioner McHugh principally relies, *Delaware River and Bay Authority v. Carello,* 43 Del. Ch. 213, 222 A.2d 794 (1966), is a totally inapposite *nisi prisus* decision. There, Delaware entered into a compact with New Jersey creating the Authority and specifically granting the Authority power to fix and determine the qualifications, duties, compensation, terms of office, pensions and all other conditions and terms of employment of its employees. When, subsequent to entering into the Compact, Delaware amended its state law to permit public employees to organize and bargain collectively, a lower court enjoined it from conducting a hearing to determine an exclusive bargaining agent for certain Authority employees. The Court ruled that the power over Authority employees granted to Authority commissioners could not be diluted by the unilateral action of one member of the Compact.

The facts in *Delaware River and Bay Authority* contrast sharply with the facts under consideration here for while Delaware specifically surrendered in the Compact its power over the terms and conditions of Authority employees, here, no party has surrendered in the WMATA Compact its power to tax persons who conduct business with the Authority. Therefore, the Maryland Court of Appeals properly concluded that *Delaware River and Bay Authority* is inapposite to this case (A. 12a n.6).

CONCLUSION

The Petition for Writ of Certiorari filed by McHugh should be denied. The questions presented by McHugh would never be decided, and two of the questions presented were not raised in the Court of Appeals. The only question that is before this Court — construction of the terms of the Compact — does not warrant review. Review would not serve any interest other than to afford McHugh one more opportunity to present an argument totally without merit. For these reasons, the State of Maryland respectfully request that the Petition for Writ of Certiorari be denied.

Respectfully submitted,

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